

**REPORT OF THE AUDITOR-GENERAL TO THE KWAZULU-NATAL PROVINCIAL
LEGISLATURE AND THE COUNCIL ON THE ETHEKWINI MUNICIPALITY
REPORT ON THE CONSOLIDATED FINANCIAL STATEMENTS**

Introduction

1. I have audited the consolidated and separate financial statements of the eThekweni Municipality and its subsidiaries set out on pages ... to ..., which comprise the consolidated and separate statement of financial position as at 30 June 2012, the consolidated and separate statement of financial performance, statement of changes in net assets and the cash flow statement for the year then ended, and the notes, comprising a summary of significant accounting policies and other explanatory information.

Accounting officer's responsibility for the consolidated financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these consolidated and separate financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Local Government: Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2011 (Act No. 6 of 2011) (DoRA), and for such internal control as the accounting officer determines is necessary to enable the preparation of consolidated and separate financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-General's responsibility

3. My responsibility is to express an opinion on these consolidated and separate financial statements based on my audit. I conducted my audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the general notice issued in terms thereof and International Standards on Auditing. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated and separate financial statements are free from material misstatement.
4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated and separate financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the consolidated and separate financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the municipality's preparation and fair presentation of the consolidated and separate financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the municipality's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated and separate financial statements.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Opinion

6. In my opinion, the consolidated and separate financial statements present fairly, in all material respects, the financial position of the eThekweni Municipality and its subsidiaries as at 30 June 2012 and their financial performance and cash flows for the year then ended, in accordance with SA Standards of GRAP and the requirements of the MFMA and DoRA.

Emphasis of matters

7. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Significant uncertainty

8. As disclosed in note 37 to the financial statements, in terms of the Municipal Property Rates Act, 2004 (Act No. 6 of 2004) ratepayers have objected to property valuations used in the computation of their property rate charge amounting to R335 million.

Material losses and impairments

9. With reference to note 48 to the financial statements, the municipality has incurred material losses relating to water and electricity amounting to R411 million and R364 million, respectively.
10. As disclosed in note 19 to the financial statements, the municipality raised a provision for bad debts amounting to R1,9 billion (2011: R1,8 billion) on consumer debts as the recoverability of these amounts is doubtful.

Irregular expenditure

11. As disclosed in note 42 to the financial statements, irregular expenditure amounting to R789 million was incurred mainly as a result of contracts awarded to suppliers, which were in contravention of the Local Government: Municipal Supply Chain Management Regulations (GNR 868 of 30 May 2005) (Municipal SCM Regulations).

Retirement benefit obligation

12. Changes in the actuarial assumptions used to value the retirement benefit obligation and post-retirement benefit medical obligation in terms of SA Standards of GRAP, GRAP 25, *Employee Benefits*, resulted in an increase of R1,2 billion in the liability as disclosed in note 5. The full amount has been recognised as expenditure in the current year in line with the municipality's accounting policy.

Restatement of corresponding figures

13. As disclosed in note 39 to the financial statements, the corresponding figures for 30 June 2011 have been restated as a result of errors discovered during 2012 in the financial statements of eThekweni Municipality at, and for the year ended, 30 June 2011.

Additional matter

14. I draw attention to the matter below. My opinion is not modified in respect of this matter.

Unaudited supplementary schedules

15. The supplementary information set out on pages xxx to xxx does not form part of the financial statements and is presented as additional information. I have not audited these schedules and, accordingly, I do not express an opinion thereon.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

16. In accordance with the PAA and the general notice issued in terms thereof, I report the following findings relevant to performance against predetermined objectives, compliance with laws and regulations and internal control, but not for the purpose of expressing an opinion.

Predetermined objectives

17. I performed procedures to obtain evidence about the usefulness and reliability of the information in the annual performance report as set out on pages ... to ... of the annual report.
18. The reported performance against predetermined objectives was evaluated against the overall criteria of usefulness and reliability. The usefulness of information in the annual performance report relates to whether it is presented in accordance with the National Treasury's annual reporting principles and whether the reported performance is consistent with the planned objectives. The usefulness of information further relates to whether indicators and targets are measurable (i.e. well defined, verifiable, specific, measurable and time bound) and relevant as required by the National Treasury *Framework for managing programme performance information*.

The reliability of the information in respect of the selected objectives is assessed to determine whether it adequately reflects the facts (i.e. whether it is valid, accurate and complete).

19. There were no material findings on the annual performance report concerning the usefulness and reliability of the information.

Additional matter

20. Although no material findings concerning the usefulness and reliability of the performance information were identified in the annual performance report, I draw attention to the following matter.

Achievement of planned targets

21. Of the total number of planned targets, only 93 were achieved during the year under review. This represents 33% of total planned targets that were not achieved during the year under review. Reasons for the non-achievement of these targets are included in the annual performance report set out on pages xxx to xxx.

Compliance with laws and regulations

22. I performed procedures to obtain evidence that the municipality has complied with applicable laws and regulations regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key applicable laws and regulations as set out in the general notice issued in terms of the PAA

are as follows:

Procurement and contract management

23. Awards were made to providers who are persons in the service of the municipality or other state institutions, which is contrary to Municipal SCM Regulation 44.
24. Contracts were modified without tabling the reasons for the proposed amendment in the council of the municipality, as required by section 116(3) of the MFMA.

Expenditure management

25. The accounting officer did not promptly in terms of section 32(4) of the MFMA inform the MEC for Local Government in the province, in writing, of the irregular expenditure incurred by the municipality and the steps that have been taken to recover or rectify such expenditure and to prevent a recurrence of such expenditure.
26. The accounting officer did not take all reasonable steps to prevent irregular expenditure, as required by section 62(1)(d) of the MFMA.

Annual financial statements

27. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Control deficiencies within the Housing and Legal unit resulted in material misstatements of current assets, revenue, expenditure, contingent liabilities, commitments and irregular expenditure, identified by the auditors that were subsequently corrected, resulting in the financial statements receiving an unqualified audit opinion.

Internal control

28. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with laws and regulations. The matters reported below under the fundamentals of internal control are limited to the significant deficiencies that resulted in findings on compliance with laws and regulations included in this report.

Financial management

29. The municipality had not implemented an effective internal control system in the form of a policy to regulate contract extensions/modifications in terms of 116(3) of the MFMA and appropriate monitoring controls to timeously prevent and detect awards to employees in service of the municipality during the year.
30. There were inadequate processes, policies and monitoring controls over financial transactions within the housing unit and legal unit. This has resulted in material misstatements identified by audit that were subsequently corrected.

OTHER REPORTS

Investigations

31. Forty-one internal investigations relating to alleged procurement fraud and non-compliance with municipal SCM regulations by council employees were finalised during the year. In addition, the forensic investigation initiated by the KwaZulu-Natal Department of Co-

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operative Governance and Traditional Affairs relating to alleged tender irregularities at the municipality was finalised and the report issued to the city manager for further action.

32. Thirty-two internal investigations relating to alleged procurement fraud, non-compliance with municipal SCM regulations and financial misconduct by council employees are in progress.

Auditor-General

Pietermaritzburg

11 December 2012



AUDITOR-GENERAL
SOUTH AFRICA

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